

Title	Trusts Funded by Court Order (adopt rule 7.903 of the California Rules of Court).
Summary	Proposed new rule 7.903 would require the probate department of the superior court, or, if there is no probate department, the judge who regularly hears proceedings under the Probate Code, to review and approve the terms of certain trusts that are funded by court order, and would require such trusts to contain certain provisions.
Source	Probate and Mental Health Advisory Committee, Hon. Thomas W. Stoevers, Chair
Staff	Douglas C. Miller, Committee Counsel, 415.865.7535, douglas.miller@jud.ca.gov
Discussion	<p>Certain trusts are funded under court orders. Some are created and funded under such orders. Others are preexisting trusts that are funded under court orders. Court-funded trusts include trusts created by probate conservators under the substituted judgment provisions of Probate Code sections 2580–2586; trusts created on petitions for authority to enter into particular transactions concerning the property of disabled spouses (Prob. Code, §§ 3100–3150); and trusts created or funded on court-approved compromises of claims or actions of minors or incompetent persons or dispositions of the proceeds of judgments for such persons under Probate Code section 3600, et seq.</p> <p>All of these trusts must be reviewed and approved by courts, either on their creation or when court approval of proposed distributions to them are requested. Most of these reviews now occur in probate proceedings and are performed by probate departments or by judges familiar with probate matters. However, civil trial judges sometimes perform these functions when actions pending in their departments involving minors or incompetent persons are settled or tried.</p> <p>The Probate and Mental Health Advisory Committee seeks to apply the experience and expertise of probate departments or judges most familiar with probate matters to the court review and approval process for all court-funded trusts.</p> <p>Many courts have local rules concerning court-funded trusts. Many of these rules require certain provisions to be included and prohibit other</p>

provisions in instruments that create these trusts.¹ There are no statewide rules concerning court-funded trusts. The advisory committee believes that a new California Rule of Court would promote greater uniformity in the content of instruments that create and govern these trusts.

Probate court review of court-funded trusts

Subdivision (b) of proposed rule 7.903 would require the probate department of the court, or the judge who regularly hears probate matters if there is no probate department, to review and approve the terms of any trust that will receive the proceeds of a compromised claim or a judgment for a minor or person with a disability under Probate Code section 3600.²

The rule would not prescribe the manner by which a particular court would obtain the review and approval of the probate department or judge. Each court would be free to determine whether all or only part of a pending case involving a minor or a disabled person that is compromised or tried should be transferred to the probate department, whether a separate petition for probate court approval should be required, or whether an informal means of securing probate department review and approval of the trust provisions of the proposed judgment or compromise will be sufficient.

There are a number of existing variations under local court rules. Los Angeles local rules provide that where a civil action is pending on the claim of a minor or incompetent person, the petition for approval of a compromise must be heard in the department where the matter is pending. If the pending civil case is settled at a settlement or pretrial conference, court approval of the compromise must be obtained from the judge who participated in that conference if he or she is available. However, if the compromise involves funding of a special needs trust—a trust with provisions that permit the trust beneficiary to

¹ See, e.g., Superior Court, County of San Bernardino Local Rules, rule 1405; Superior Court, County of Fresno Local Rules, rule 82.16; Superior Court, County of Contra Costa Local Rules, rule 1002; Superior Court, County of Los Angeles Local Rules, rules 10.186 and 10.186.1; and Superior Court, County of Orange Local Rules, rule 611.08.

² Section 3600 refers to a minor or an “incompetent person.” The latter term is not precisely defined but includes a person for whom a conservator could be appointed (Prob. Code, § 3603). The proposed rule substitutes “person with a disability” for “incompetent person” to be consistent with pending legislation sponsored by the State Bar’s Trusts and Estates Section that would amend section 3600–3612, et seq., including section 3603. (Assem. Bill No. 1851 (2003–2004 Reg. Sess.), § 4, introduced by Assembly member Harman on January 29, 2004.)

receive distributions from the trust while retaining eligibility for needs- or age-based public benefits—or a trust for a minor that becomes revocable when the minor turns 18, review and approval of the terms of the trust by the probate department is required. The rules do not require formal assignment or transfer to the probate department or the filing of a separate petition in that department for this purpose.³

A Sacramento local rule provides that if the proceeds of a proposed judgment or compromise in favor of a minor or an incompetent person are to be placed in any kind of trust, the assigned (civil) department must first enter judgment or approve all other matters, including the amount of the settlement, terms of payment, and attorney fees. The petitioner must then file a petition in the probate department for a hearing on the establishment, terms, and conditions of the proposed proceeds disposition.⁴

A Stanislaus local rule is procedurally identical to the Sacramento rule described above but requires probate court review and approval only for special needs trusts.⁵

Subdivision (b) of proposed rule 7.903 would require that a trust described in that subdivision must be subject to the continuing jurisdiction of the court and may be subject to court supervision similar to the supervision of a decedent's estate proceeding as the court may order. This provision is based on similar language in Probate Code section 3604 applicable to special needs trusts, but would apply to all court-funded trusts that will receive the proceeds of a judgment or compromise under Probate Code section 3600, et seq.

Required provisions in court-funded trusts

Rule 7.903(c) would provide that trust instruments for all court-funded trusts defined in subdivision (a) of the rule must contain certain provisions and may not contain no-contest clauses unless the court otherwise orders for good cause shown. The required provisions are conservative but the court would be given the flexibility and discretion to otherwise order if a case for dispensing with any of the required provisions or permitting a no-contest clause can be made in the

³ Superior Court, County of Los Angeles Local Rules, rules 10.186.2 and 10.187.

⁴ Superior Court, County of Sacramento Local Rules, rule 15.105.

⁵ Superior Court, County of Stanislaus Local Rules, rule 8.140.

circumstances of a particular case.

The required provisions include bonds for trustees and others given authority under the trust instrument to direct the trustee to make disbursements, a direction to the trustee to file accounts and reports for court approval in the manner and frequency required for a conservator of the estate and a personal representative of a decedent's estate, a requirement for court approval of changes of trustee and a court order appointing a successor trustee, a requirement that the compensation of the trustee, the trustee's attorney, and the members of any advisory committee be in just and reasonable amounts to be fixed and allowed by the court.

The rule would also require trust instruments to prohibit trust investments other than those permitted conservators of the estate under Probate Code section 2574. This is a more conservative investment philosophy than is permitted for private trusts under the Uniform Prudent Investor Act (Prob. Code, §§ 16045–16054). The advisory committee is concerned that the Act is too vague and general to be routinely applied to court-funded trusts, but recognizes that a court may permit greater investment flexibility if the circumstances in a particular situation would support the exercise of that discretion.

A copy of proposed rule 7.903 is attached at pages 5–6.

Attachment

Rule Proposal

Rule 7.903, in title 7 of the California Rules of Court, would be adopted, effective January 1, 2005, to read:

Rule 7.903. Trusts funded by court order

(a) Definition

“Trust funded by court order” under this rule means and refers to a trust that will receive funds under Probate Code sections 2580, et seq. (substituted judgment); 3100, et seq. (proceedings for particular transactions involving disabled spouses or registered domestic partners); or 3600, et seq. (settlement of claims or actions or disposition of judgments involving minors or persons with disabilities).

(b) Review of certain trusts by probate department or judge

The probate department of the court or, in a court that does not have a probate department, the judge who regularly hears proceedings under the Probate Code, must review and approve the terms of any trust that will receive the proceeds of a proposed settlement of a claim or pending action or a judgment for a minor or person with a disability under Probate Code section 3600, or will receive such proceeds on later application of the minor or person with a disability under Probate Code section 3604. The trust must be subject to the continuing jurisdiction of the court, and may be subjected to court supervision as the court may order.

(c) Required provisions in trust instruments

Unless the court otherwise orders for good cause shown, trusts instruments for trusts funded by court order must:

- (1) not contain “no-contest” provisions;
- (2) clearly identify the trustee and any other person with authority to direct the trustee to make disbursements and require such persons to post bond in the amount required under Probate Code section 2320, et seq.;
- (3) require the trustee to file accounts and reports for court approval in the manner and frequency required by Probate Code sections 1060, et seq. and 2320 et seq.;

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2 (4) require court approval of changes in trustees and a court order appointing any
3 successor trustee;
4
5 (5) prohibit investments by the trustee other than those permitted under Probate
6 Code section 2574;
7
8 (6) require compensation of the trustee, the members of any advisory committee,
9 or the attorney for the trustee, to be in just and reasonable amounts, to be fixed
10 and allowed by the court. The instrument may provide for periodic payments
11 of compensation on account, subject to the requirements of Probate Code
12 section 2643 and rule 7.755.